



CBN 5-YEAR POLICY THRUST: IMPLICATIONS FOR THE CAPITAL MARKET

POLICY BRIEF

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1. INTRODUCTION

The Governor of the Central Bank of Nigeria (CBN), Mr. Godwin Emefiele, unveiled the Bank's five-year vision and policy thrust on June 24th, 2019. The CBN's five-year economic plan will largely hinge on efforts at promoting price, monetary, exchange rate and financial system stability as well as stimulating growth through development finance interventions. The CBN Governor further outlined the strategies through which the Bank intends to achieve the priority objectives.

Specifically, the five-year plan identified five major priority areas the CBN would concentrate on:

- i. *Preserve domestic macroeconomic and financial stability.*
- ii. *Foster the development of a robust payments infrastructure system that will increase access to finance for all Nigerians thereby raising the financial inclusion rate.*
- iii. *Improve access to credit to small holder farmers, Medium, Small and Micro Enterprises (MSMEs), Consumers, mortgage facilities for bank customers, entrepreneurship skills in the creative industry and the education sector.*
- iv. *Grow external reserves*
- v. *Support efforts at diversifying the economy through intervention programmes in the agriculture and manufacturing sectors.*

Therefore, the aim of this Policy Brief is to provide a summary of the CBN's strategies for achieving its five-year policy thrust and draw relevant implications for the capital market.

2. SUMMARY OF THE 5-YEAR VISION

2.1 MACROECONOMIC STABILITY

The CBN plans to use monetary policy tools to encourage low inflation and maintain a stable exchange rate. The monetary policy

measures taken during the period will be aimed at reducing inflationary pressures, supporting improved productivity in the agricultural and manufacturing sectors as well as facilitating improved access to credit and a corresponding growth in output and employment.

2.2 EXCHANGE RATE STABILITY

The CBN will continue to operate a managed float exchange rate system. It also intends to support efforts towards the diversification of the country's export base as well as improve non-oil export and reserve accretion.

2.3 FINANCIAL SYSTEM STABILITY

The CBN intends to achieve the stability of the financial institutions and innovation by enhancing its on-site and off-site supervision of all financial institutions to improve risk management in all aspects of the financial sector. In the plan also is the recapitalization of the banking sector to position the banks among the top 500 in the world as well as improve the cybersecurity of financial channels.

2.4 ROBUST PAYMENT SYSTEM INFRASTRUCTURE

This aspect of the policy reinvigorates the drive towards cashless policy, financial inclusion and digitalization of financial services. A main objective is to improve the dynamism, security and efficiency of digital payment channels and thus will be carried out in conjunction with Fintech and other financial agents.

2.5 TARGETED DEVELOPMENT FINANCE

The CBN will target specific sectors of the economy for development. Among the plans proffered are:

- *Boosting agricultural productivity of different food crop commodities to reduce importation and increase employment and non-oil exports.*
- *Provision of better financial facilities for farmers through anchor borrowers' program and credit bureaus.*

- Increased support for research and development on improved and enhanced farming practices.
- Discouraging the activities of smugglers who bring in restricted goods into the country by blacklisting and denying perpetrators and their affiliated companies' access to banking services in the entire country.

2.6 FINANCIAL INCLUSION

The CBN, over the next five years also plans to broaden access to financial services to individuals in the underserved part of the country. The ultimate goal is to ensure that 95% of eligible Nigerians have access to financial services by 2024. The bank will also strengthen its consumer protection mechanism as well as intensify financial literacy campaigns.

2.7 ACCESS TO CREDIT

The CBN plans to encourage financial institutions to channel credit to critical sectors of the economy, especially MSMEs, agriculture and real estate sectors to support their growth. MSMEs, which constitute over 90% of businesses in Nigeria, have registered over N400bn worth of movable assets through the collateral registry. The CBN plans to triple this figure in the next three years, which will broaden the range of collateral and improve access to credit.

2.8 UNIQUE IDENTIFICATION

The CBN will support an aggressive enrolment of prospective banking customers in the informal sector onto the BVN system. The current enrolment of 38 million unique banking customers will be expanded to 100 million over the next 5 years. The ongoing partnership with National Identity Management Commission (NIMC) will also enable integration between the two databases. This will encourage the development of a credit profile for banking customers and provide banks reassurance in providing services to large customer base.

2.9 LENDING TO MSMEs

The Nigeria Incentive-Based Risk-Sharing System for Agricultural Lending (NIRSAL)

Microfinance Bank will work towards providing rural communities access to funding. To complete this, the CBN will support the development of a trade receivables portal which will facilitate the trading of MSMEs' receivables with financial institutions. This will increase cash flows and reduce high account receivables issues affecting MSMEs' production and growth.

2.10 CONSUMER CREDIT

The CBN identifies consumer credit as critical to economic growth, improved consumer spending and accelerated investments. Currently, less than 10% of Nigerians that have bank accounts utilise banks' financial products like credit cards and personal loans. To encourage lending to consumers, the CBN will develop a lending framework which will allow departmental stores, equipment leasing companies and others, in partnership with financial institutions, to offer credit to consumers at reasonable rates.

2.11 MORTGAGE LENDING

In an effort to support the growth of the real estate industry, the CBN will develop a framework that will allow banks to securitize mortgage loans and sell in the capital market. It is believed this will reduce credit and liquidity risk to banks as well as increase the expanse of funds available for mortgage loans. It will also reduce the cost of obtaining mortgages for customers.

3. IMPLICATIONS FOR THE NIGERIAN CAPITAL MARKET (NCM)

The policy objectives outlined will have an impact on the Nigerian Capital Market, some of which are discussed below:

1. **Macroeconomic Stability:** a stable macroeconomic environment will boost economic growth and capital market performance usually mirrors a country's general economic performance. A stable macroeconomic environment will therefore be good for the capital market and foreign investment. Benefits also exist for listed companies especially those involved in

manufacturing and agricultural activities. However, the CBN plan shows that interest rates will remain high as long as high inflation persists. This often engenders preference for investment in fixed income securities over equities and makes FGN instruments crowd out the private sector.

2. Exchange Rate Stability: currency fluctuations directly and indirectly affect several macroeconomic outcomes and objectives especially in the area of international trade and finance. A stable exchange rate may encourage inflow of portfolio investments and enhance market liquidity. It will also lead to less uncertainty for importing and exporting quoted firms. However, since managing a country's currency comes at a cost, the extent to which these benefits can be realised depends on assurance of a constant flow of foreign exchange especially through improved crude oil production and price.

3. Financial System Stability: recapitalization will give additional buffers for the financial institutions and give them the ability to better provide funding and compete in the global space. For instance, in 2005, the CBN required banks to raise their capital base from ₦2bn to ₦25bn which was equivalent to \$250m. It was estimated that over ₦400bn was raised through the capital market and at the end of the exercise 25 banks emerged out of the 89 that existed prior to the recapitalization. However, following the depreciation of the naira over several years, banks' capital has fallen substantially below \$250m, to about \$69.4m. Although the CBN has not disclosed how much increase in capital it is targeting, it is expected that some banks will raise funds through the capital market. Recapitalization therefore will increase the liquidity and capitalization of the NCM, as the financial sector is the most liquid sector on the stock exchange. Given the consideration of recapitalization by the

Insurance and now the Banking sector, the capital market regulator may also need to evaluate the capital adequacy of the operators in the market.

4. Robust Payment System: an important function of the financial system is to facilitate the allocation and deployment of resources and this encompasses the payment system through which financial transactions are settled. Having an efficient and safe payment system promotes financial system and economic growth. The capital market needs a robust payment system to thrive. It can therefore leverage the CBN's payment system to drive some of its initiatives for developing the market. Some capital market products and initiatives, such as derivatives, retail bond trade, Direct Cash Settlement (DCS), among others, cannot thrive without a safe and efficient payment system. This also lends credence to the recent interest the NCM is giving to the players and products in the Fintech space as a tool to deepening the market.

5. Targeted Development Finance: this policy has the potential to raise agricultural productivity, income and standard of living of targeted farmers as well as lead to job creation in the sector. Agricultural firms listed on the stock exchange that may benefit from the policy will likely experience higher valuation. It will also complement the current efforts at developing a commodity exchange eco-system. Currently, AFEX, Lagos Commodity and Futures Exchange and NCX are doing a lot in the area of commodity trading in Nigeria. These platforms can be used to advance credit to small-holder farmers, facilitate price discovery and encourage off-take of farmers' produce.

6. Financial Inclusion: the NCM can collaborate with the CBN to incorporate specific topics on capital market financial inclusion initiatives as

part of the general financial literacy programme. It is believed that this will boost retail investors' participation in the market.

7. **Access to Credit:** the NCM also needs to develop ways of leveraging the assets in the collateral registry to structure capital market products.
8. **Unique Identification:** the current KYC used in the NCM leverages the BVN which has also been used to drive the e-Dividend initiative. Expanded BVN information can also be used to raise the number of retail investors in the NCM. There is also the need for capital market operators to be uniquely identified as this is necessary for the success of initiatives like e-Dividend, DCS and multiple subscriptions.
9. **Lending to MSMEs:** the NCM can be made a source of financing to MSMEs through both the traditional and innovative channels. Traditional methods are through private equity, venture capital, and Alternative Securities Market (ASeM). Innovative channels include crowdfunding and operations of commodity exchanges. The MSMEs' receivables can be the underlying for a class of asset which can be traded in the capital market. Thus, relevant platforms can be registered by the Commission to key into this initiative of the CBN.
10. **Consumer Credit:** in addition to consumer credit, it is also important to look into retail investment. There is a need to improve the variety of products and services available to retail investors, and part of this is being addressed by some capital market initiatives such as the issue of margin lending. More engagement is therefore required with the CBN to allow banking stocks be included as part of marginable securities as well as see to it that the exiting list is updated.
11. **Mortgage Lending:** This policy will help broaden capital market products available for investors, enabling them

to manage risks through diversification. Currently, there are two Real Estate Investment Trust (REIT) schemes, UPDC REIT and Union Homes REIT and about six Mortgage Banks listed on the Nigerian Stock Exchange. Furthermore, the Nigeria Mortgage Refinance Company raised up to ₦11bn worth of assets from the capital market to refinance the mortgage portfolio of member Primary Mortgage Banks to enhance housing finance in the country. Thus, the market can support this initiative. This is also an opportunity to unlock derivatives trading in the market.

4. CONCLUSION

The policy brief has given a summary of the CBN's vision in the next five years which aims to promote price, monetary, exchange rate and financial system stability as well as support economic growth through various intervention programmes. Some of the bank's policies directly or indirectly affect the NCM and these have also been discussed. Considering the impact of the policy on the NCM, it is therefore important that the capital market community take advantage of the areas that impact the capital market. It is also critical for the capital market regulator to develop channels of collaboration and engagement with the CBN especially on sector specific issues that have a direct impact on the capital market.